

STATE OF TENNESSEE



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Commentary on the State Pooled Investment Fund

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Money market funds, like the State Pooled Investment Fund (SPIF), were designed to be safe places to invest cash. The investment goals of the SPIF are safety, liquidity, and return, in that order. Money market funds are designed to have a stable Net Asset Value (NAV) of \$1.00, therefore if you invest a dollar, you should receive a dollar plus some earnings in return. These funds were designed to have no tolerance for risk.

Several money market funds have run into trouble because some of their instruments lost value. During the summer and fall of 2007, funds that had investments in Collateralized Debt Obligations (CDO's) or Structured Investment Vehicles (SIV's) saw those investments lose much of their value. Recently, because of the bankruptcy of Lehman Brothers and the troubles that other members of the financial industry have experienced, we have seen other money market funds have problems. On September 16, the Primary Reserve Fund, a \$65 billion money market fund "broke the buck", or became worth less than \$1 per share. This was due to a large holding of Lehman Brothers commercial paper that was valued at zero after the firm filed bankruptcy.

There have been other companies in the news lately that are common household names. Companies like Merrill Lynch, AIG, Fannie Mae, Freddie Mac, Morgan Stanley, and Washington Mutual have all been in the headlines. I wanted to take this opportunity to let you know that the SPIF has no direct credit exposure to any of the securities that have experienced difficulties during this time. The SPIF is invested in collateralized bank deposits, US governments and agencies, and commercial paper. The commercial paper held in the SPIF must be rated in the highest category by at least two of the nationally recognized ratings organizations, it must mature within 45 days, and no asset backed commercial paper is allowed. Although there are investments in Fannie Mae and Freddie Mac, there are no investments in their mortgage backed securities or their preferred stock.

All bank deposits of the SPIF are collateralized. Deposits in banks that participate in the Collateral Pool Program are collateralized to a target amount. If there is a bank failure of a participating bank, any uncollateralized exposure is guaranteed by the other participating banks. All other bank deposits are collateralized at 105%. The collateral is highly liquid and is marked to market daily, or as often as the security is priced. The pricing service that is utilized is IDC, a highly regarded source in the industry.

The investment policy for the SPIF is designed to minimize risk and since inception, the SPIF has never experienced a realized loss due to credit risk.

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